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BEFORE THE ARIZONA CORPORATION COMMISSION

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GARY PIERCE, Chairman  
PAUL NEWMAN  
SANDRA D. KENNEDY  
BOB STUMP  
BRENDA BURNS

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AZ CORP COMMISSION  
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IN THE MATTER OF THE APPLICATION OF  
ARIZONA PUBLIC SERVICE COMPANY FOR  
A HEARING TO DETERMINE THE FAIR  
VALUE OF THE UTILITY PROPERTY OF THE  
COMPANY FOR RATEMAKING PURPOSES,  
TO FIX A JUST AND REASONABLE RATE OF  
RETURN THEREON, AND TO APPROVE RATE  
SCHEDULES DESIGNED TO DEVELOP SUCH  
RETURN

DOCKET NO. E-01345A-11-0224

NOTICE OF FILING TESTIMONY

AARP hereby files the attached testimony of Nancy Brockway Supporting Settlement Agreement.

RESPECTFULLY SUBMITTED on January 17, 2012.

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6 By:   
7 Craig A. Marks

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**TESTIMONY  
OF  
NANCY BROCKWAY  
ON BEHALF OF AARP  
SUPPORTING SETTLEMENT AGREEMENT  
JANUARY 18, 2012**

### **EXECUTIVE SUMMARY**

The Settlement Agreement addresses the concerns about pre-approval and decoupling that I raised in my earlier testimonies. I recommend that the Settlement Agreement be approved. It contains specific benefits and protections for residential, fixed-income and low-income customers. On balance, it provides a just and reasonable resolution of the Company's rate case.

First, under the Settlement Agreement, the Company agrees to withdraw its request for the so-called Environment and Reliability Account. The ERA would have amounted to a form of pre-approval for plant investment, and would have undermined the ability of the Commission to determine the prudence of such investments.

Second, APS has agreed to a targeted decoupling mechanism (called the "Lost Fixed Cost Recovery" mechanism" or "LFCR"), whereby it will recover a portion of verified, unrecovered distribution and transmission costs resulting from its energy efficiency programs, instead of an unlimited decoupling mechanism as originally proposed. In this fashion, the Company continues to bear those risks which it is better able to manage, such as weather variations, rather than shifting those risks to consumers. At the same time the Company will receive limited cost recovery based on its verified energy savings pursuant to the state's energy efficiency goals. The LFCR mechanism will be applied equally to all kilowatt-hours, thus preserving an incentive to save energy. In addition, the Settlement Agreement contains an opt-out provision, allowing customers who prefer to take service under rates designed to recover assigned revenues less on a usage basis than is the case with regular rates subject to the LFCR adjustment. APS agrees to work with interested parties to design and implement an outreach program to inform customers of this option.

An additional benefit of the Settlement Agreement is that APS customers would not bear the \$85.9 million dollar net increase to revenue APS requested in its updated revenue request. The net impact of the Settlement Agreement on base rates as of the day the new rates take effect will be a slight decrease for most residential customers, and the Company agrees not to implement any new general rate increase before July 1, 2016, effectively a four-year stay-out (subject to certain conditions). Before that date, it is true that rates may increase as a result of changes in the effect of various tracker rates, and the possible inclusion of the Four Corners purchase. However, the Company agrees not to increase rates under these tracker rates before 2013. Thus, overall rates will remain stable through the end of the year.

On rate design issues, Settlement Agreement significantly amends the Company's original restructuring of the low-income discount rates, to preserve the average level of rate relief now provided, and to maintain the tiered discount system, whereby lower-usage customers receive a greater discount level. These amendments make it possible to concur with the underlying proposal to simplify the structure of the low-income rates, as proposed in the APS filing, while also addressing the concerns raised in my testimony. APS has also agreed to leave the basic service charges intact, which prevents the unreasonable shifting of revenue responsibility to low-

usage customers about which I expressed concern in my rate design testimony. The inverted block effect of the low-income rate design, retained by the Settlement Agreement, will have a positive effect on customer incentives to conserve energy.

Finally, the Settlement Agreement adds a residential hold-harmless provision to the proposed wholesale (or "buy-through") purchase provision for large customers, the so-called AG-1 rate. As filed, there was no protection against the Company seeking to make residential customers pay towards any costs "stranded" as a result of large customer switch to this new rate. The Settlement Agreement makes clear that residential customers will not have to bear any increased costs as a result of the implementation of the AG-1 rate.

**I. INTRODUCTION AND PURPOSE**

**Q. ARE YOU THE SAME NANCY BROCKWAY WHO FILED TESTIMONY IN THIS DOCKET ON NOVEMBER 18, 2011 AND DECEMBER 2, 2011?**

A. Yes.

**Q. WHICH PARTY IS SPONSORING YOUR TESTIMONY?**

A. AARP is sponsoring my testimony in this docket.

**II. THE APS SETTLEMENT AGREEMENT**

**Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY FILED TODAY?**

A. In this testimony, I explain why the proposed Settlement Agreement, filed January 6, 2012, is in the public interest. Specifically, I will discuss how the Settlement Agreement compares to the original filing, and in particular how it addresses the concerns I raised in my revenue-requirement and rate-design testimonies in this docket. I will describe the net benefits that the Settlement Agreement brings to residential customers.

**Q. PLEASE SUMMARIZE YOUR TESTIMONY CONCERNING THE APS PROPOSALS ON REVENUE REQUIREMENT IN THIS DOCKET.**

A. In my November 18, 2011, testimony, I made the following points concerning the APS proposals on revenue requirements, including the APS full decoupling proposal:

The Commission should reject APS' proposed ERA and EIA tracking accounts.

1. The ERA generation-addition cost tracker is not needed in order for APS to recover its costs of service and earn a fair return. APS proposes that the present APS Environmental Improvement Surcharge ("EIS") be replaced by what it calls the Environmental and Reliability Account ("ERA"). Between rate cases, APS would book to that account the costs of certain new generation additions and additional pollution controls for existing generation, and then recover these costs in tracker rates reset annually outside a rate case, until the next base rate case. The Company claims it needs to adjust rates whenever a generation addition or

environmental compliance investment is made, or else its earnings will be eroded. The Company fails to acknowledge that many changes occur after any given rate case, and increases in revenue requirements in one area (such as generation additions) may be offset by decreases in revenue requirement elsewhere (as in depreciation accounts). Only an updated and comprehensive estimate of revenue requirements can determine whether raising rates to explicitly reflect a given plant investment will create excess earnings. Further, the tracker mechanism will make prudence determinations difficult if not practically impossible. The ERA is not needed, and its institution would shift significant risks from the Company to the consumer, yet APS does not propose to reduce its requested return to acknowledge this fact. The ERA should be rejected.

2. The EIA (decoupling mechanism) is not necessary to assure fair and vigorous investments by APS in energy efficiency and unfairly shifts risks, such as economic downturns, to ratepayers. APS presents its EIA as necessary to facilitate its investments in and support for energy usage reduction measures. However, APS proposes a full decoupling mechanism that would protect its revenues as sales erode for any reason, including non-utility efficiency initiatives, economic downturns, or weather. Decoupling, and removal of the direct incentive for APS to sell more electricity does not guarantee that APS will invest in effective energy efficiency measures and demand-side management programs in which all APS customers can benefit. Further, adoption of revenue decoupling is not a necessary or sufficient condition to increase energy efficiency. There are numerous, non-decoupling tools available to public policy-makers to promote energy efficiency objectives. Decoupling will shift significant risks from APS to its consumers, yet APS does not propose to reduce its requested return to reflect this reality. APS is in a better position than consumers to manage weather-related risks. APS should not be made whole for sales reductions caused by service interruptions or outages. The APS mechanism rate design does not promote energy efficiency. The APS EIA proposal should be rejected.

**Q. PLEASE SUMMARIZE YOUR TESTIMONY CONCERNING THE APS PROPOSALS ON RATE DESIGN IN THIS DOCKET.**

A. In my December 2, 2011, testimony, I made the following points concerning the APS proposals on rate design in this docket:

The Company's proposed changes to the structure of the low-income rates are not advisable and should be rejected. APS should not add to the low-income revenue responsibility (PSA, DSMAC and TCA), and then apply a flat 25% discount to the resulting higher bill regardless of usage. The Company also should not



increase the underlying base rates for Low Income rates by a percentage any higher than the percentage increases on the corresponding non-low-income rates. Instead, the present structure of the low-income rates should be retained. That is, the tiered discounts and exemptions from PSA and DSMAC riders should be retained. The underlying Low-Income base rates should be increased by the same percentages as those on the corresponding non-low-income base rates. The cap on the discounts should also be increased by the same percentage. To mitigate potential burdens of higher base rates on higher usage lower income customers, special efforts should be made to target efficiency programs to such customers.

The Company's proposed increases to basic service charges should be rejected. These increases fall hardest on low-use customers, many of whom are low-income. Increasing basic service charges is inconsistent with the goal of providing price signals for energy conservation.

**Q. HOW DOES THE SETTLEMENT AGREEMENT ADDRESS YOUR CONCERNS ABOUT THE REVENUE REQUIREMENTS ISSUES IN THIS DOCKET?**

A. The Settlement Agreement addresses both of my concerns regarding the revenue-requirements issues. First, the Company has agreed to withdraw its request for the so-called Environment and Reliability reconciling tracking account. Second, APS has agreed to a targeted decoupling mechanism (called the "Lost Fixed Cost Recovery" mechanism" or "LFCR"), whereby it will recover a portion of verified, unrecovered distribution and transmission costs resulting from its energy efficiency programs, instead of an unlimited decoupling mechanism as originally proposed. In this fashion, the Company continues to bear those risks which it is better able to manage, such as weather variations, rather than shifting those risks to consumers. At the same time the Company will receive limited cost recovery based on its verified energy savings pursuant to the state's energy efficiency goals. The LFCR mechanism will be applied equally to all kilowatt-hours, thus preserving an incentive to save energy.



In addition, the Settlement Agreement contains an opt-out provision, allowing customers who prefer not to pay a lost fixed cost adjustment to take service under rates designed to recover assigned revenues less on a usage basis than is the case with regular rates subject to the Lost Base Revenue adjustment. APS also agrees to work with interested parties to design and implement an outreach program to inform customers of this option.

**Q HOW DOES THE SETTLEMENT AGREEMENT ADDRESS YOUR CONCERNS ABOUT THE RATE DESIGN ISSUES IN THIS DOCKET?**

A. The Settlement Agreement significantly amends the Company's original restructuring of the low-income discount rates, to preserve the average level of rate relief now provided, and to maintain the tiered discount system, whereby lower-usage customers receive a greater discount level. These amendments make it possible to concur with the underlying proposal to simplify the structure of the low-income rates, as proposed in the APS filing, while also addressing the concerns raised in my testimony. APS has also agreed to leave the basic service charges intact, which prevents the unreasonable shifting of revenue responsibility to low-usage customers about which I expressed concern in my rate design testimony. The inverted block effect of the low-income rate design, retained by the Settlement Agreement, will have a positive effect on customer incentives to conserve energy.

**Q. ARE THERE OTHER BENEFITS FOR RESIDENTIAL CUSTOMERS IN THE SETTLEMENT AGREEMENT?**

A. Yes. Under the Settlement Agreement, APS customers will not bear the increase to revenue APS requested in its updated revenue request. The net impact of the Settlement Agreement on base rates as of the day the new rates take effect will be a slight decrease

for most residential customers, and the Company agrees not to implement any new general rate increase before July 1, 2016, effectively a four-year stay-out (subject to certain conditions). Before that date, it is true that rates may increase as a result of changes in the effect of various tracker rates, and the possible inclusion of the Four Corners purchase. However, the Company agrees not to increase rates under these tracker rates before 2013. Thus, overall rates will remain stable through the end of the year.

**Q. ARE THERE ADDITIONAL BENEFITS FOR RESIDENTIAL AND LOW-INCOME CUSTOMERS IN THE SETTLEMENT AGREEMENT?**

A. Yes. The Settlement Agreement adds a residential hold-harmless provision to the proposed wholesale (or "buy-through") purchase provision for large customers, the so-called AG-1 rate. As filed, there was no protection against the Company seeking to recover from residential customers any costs "stranded" as a result of large customer switch to this new rate. The Settlement Agreement makes clear that residential customers will not have to bear any increased costs as a result of the implementation of the AG-1 rate.

**Q. WHY IS IT IMPORTANT THAT THE SETTLEMENT AGREEMENT PROTECT RESIDENTIAL RATEPAYERS FROM CLAIMED LOST GENERATION REVENUES ASSOCIATED WITH THE AG-1 RATE?**

A. The AG-1 rate allows large customers to obtain service under market-based rates. To the extent that APS has already committed resources to generation more costly than what is available in the market, APS may claim that it must be made whole for the difference between the price paid under the AG-1 buy-through and APS's costs of generation. The

proposed new rate is intended to benefit large customers. Residential consumers will not be responsible for any generation revenue shortfalls APS may claim as a result of the implementation of AG-1. It is only fair, then, that they not be required to pay any portion of any future alleged shortfalls. This provision added to the AG-1 proposal is a crucial element in order to protect residential customers.

**Q. ARE THERE FURTHER BENEFITS FROM THE SETTLEMENT AGREEMENT?**

A. Yes. The Agreement provides that any funds remaining of the \$5 million funding for low-income assistance as required in the last rate case may be used to assist customers whose incomes are less than or equal to 200% of the Federal Poverty Income Guidelines. It is well understood that 100% of the Federal Poverty Guideline does not identify all the households in need. This provision will expand the usefulness of the funding already agreed to. Also, the Company agrees to convene a working group to develop a more straightforward bill format. Through this process it may be possible to reduce confusion for customers about their electric bills.

**Q. DO YOU RECOMMEND THAT THE COMMISSION APPROVE THE SETTLEMENT AGREEMENT?**

A. Yes.

**Q. WHY DO YOU RECOMMEND THAT THE COMMISSION APPROVE THE SETTLEMENT AGREEMENT?**

A. The Settlement Agreement represents a sensible and reasonable resolution of the issues presented in the APS request for a general rate increase. As far as I am aware, it follows

the precedents of this Commission. As is the case with all settlements (and for that matter most Commission orders or other dispositions of a rate case), the Settlement Agreement contains some elements that I and AARP would have preferred not to see implemented, and neglects to include some elements that I would have preferred to see adopted. On balance, however, it resolves the rate case issues in a way that is just and reasonable to all parties.

**Q. DOES THIS CONCLUDE YOUR TESTIMONY ON THE SETTLEMENT AGREEMENT?**

**A. Yes.**